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No. 91-1630

Supreme Court, U.S.
FILED
MAY 8 1992
OFFICE OF THE CLERK

In The

Supreme Court of the United States

October Term, 1991

ROBERT E. KING,

Petitioner,

v.

NCNB TEXAS NATIONAL BANK, N/K/A NATIONSBANK OF TEXAS, N.A., SUCCESSOR IN INTEREST TO FIRST REPUBLICBANK DALLAS, SUCCESSOR IN INTEREST TO INTERFIRST BANK DALLAS, N.A.,

AND

FEDERAL DEPOSIT INSURANCE CORPORATION AS RECEIVER FOR FIRST REPUBLICBANK DALLAS, N.A.,

Respondents.

Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Fifth Circuit

BRIEF OF RESPONDENT NCNB IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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QUESTION PRESENTED

Whether the doctrine and principles of federal common law, as defined in *D'Oench, Duhme & Co. v. FDIC*, 315 U.S. 447 (1942), and its progeny, apply to bar claims based upon alleged oral promises and representations made by employees of a failed bank that are asserted by Petitioner as constituting violations of the Bank Tying Act, 12 U.S.C. §§ 1971-1978.

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OPINIONS BELOW

The opinion of the Court of Appeals is unreported. [Petition for Writ of Certiorari ("Pet."), Appendix ("App.") A.] The Order Granting Motions for Summary

Judgment and Final Judgment are unreported. (App. B and C, respectively).

JURISDICTION

The Fifth Circuit entered judgment on December 10, 1991. This Court extended the time for filing a petition for writ of certiorari in this matter through April 8, 1992. Petitioner filed his Petition for Writ of Certiorari on April 8, 1992. Jurisdiction of the Court is invoked under 28 U.S.C. § 1254(1).

STATEMENT OF THE CASE

Petitioner Robert E. King ("King") states that Respondent NCNB Texas National Bank, n/k/a NationsBank of Texas, N.A., ("Respondent NCNB") did not take issue with any of the facts asserted by King in the trial court. (Pet. 3 at n. 1). While Respondent NCNB does not take issue with Petitioner's Statement in most respects, Respondent NCNB would point out the following misleading statements, omissions and inaccuracies contained in Petitioner's Statement.

In response to NCNB's Motion for Summary Judgment below, King submitted the Affidavit of Robert E. King ("King Affidavit") in Opposition to Motion for Summary Judgment. (R. Vol. 12, pp. 2874-87). Attached to the King Affidavit is an unauthenticated loan committee memorandum of InterFirst Bank, Dallas ("InterFirst"). (R.

Vol. 12, pp. 2881-87). In Petitioner's Statement to this Court, King represents that:

> [t]he facts underlying petitioner's claims and defenses based upon tying violations were memorialized in an internal InterFirst memorandum. This memorandum, which was part of InterFirst's files, described the basic terms of the agreement which petitioner was coerced to enter.

(Pet. 5)

As this Court will see from a review of the King Affidavit and the internal memorandum attached thereto, King's Bank Tying Act claims are wholly based upon oral promises not reflected in the bank's records. The King Affidavit expressly states in pertinent part that the memorandum "does not state that this agreement was being forced on me." (R. Vol. 12, p. 2878). Moreover, the memorandum attached to the King Affidavit does not contain any written conditions as alleged by King to be in violation of the Bank Tying Act that were required by InterFirst to facilitate the $1,065,000.00 Promissory Note in question, nor does the memorandum refer to any oral promises or representations.

Thus, as the district court and Fifth Circuit correctly analyzed, the linchpin of King's Bank Tying Act claim is wholly dependent upon alleged oral promises or representations made by the officers of InterFirst to King to induce him to execute the loan documents. (R. Vol. 12, p. 2922; App. A 6a). The district court held that "[t]he very essence of King's claim concerns alleged oral promises made by the officers of InterFirst to King to provide financing for his other businesses." (App. B 18a).

At the district court level King asserted numerous affirmative defenses and counterclaims including, *inter alia*, duress. (App. B 12a). However, on appeal to the Fifth Circuit, King argued only that the district court erred in holding that his Bank Tying Act claim was barred by *D'Oench, Duhme* because the district court's holding somehow nullifies or repeals the Bank Tying Act. (App. A 5a-6a). Thus, Petitioner's claims and arguments relating to economic duress were abandoned and are not properly before this Court.

SUMMARY OF ARGUMENT

The district court, as affirmed by the Fifth Circuit, correctly held that King's Bank Tying Act claims were barred by the *D'Oench, Duhme* doctrine. Like all of King's other affirmative defenses and counterclaims, his Bank Tying Act claims are based on oral representations and promises allegedly made by representatives of InterFirst. Such claims give rise to the classic application of the *D'Oench, Duhme* doctrine.

As noted in the Fifth Circuit's decision, the application of the *D'Oench, Duhme* doctrine does not negate, nullify or repeal the Bank Tying Act; it merely recognizes that a private claim thereunder, which is based on unrecorded agreements or representations, cannot be asserted against the Federal Deposit Insurance Corporation ("FDIC") or its assignees. (App. A 7a). Thus, the application of the *D'Oench, Duhme* doctrine in this case is in accord with basic principles recognized by this Court regarding the scope of the doctrine and its statutory

counterpart, 12 U.S.C. § 1823(e). Further, such application does not conflict with the policies and purposes underlying the Bank Tying Act.

REASONS FOR NOT GRANTING THE WRIT

I. THE DECISION OF THE FIFTH CIRCUIT IS IN ACCORD WITH GOVERNING STATUTORY LAW AND THE PRECEDENT OF THIS COURT

The *D'Oench, Duhme* doctrine, as originally stated, holds that when a federally insured bank fails, borrowers of the bank may not later defend against collection efforts of a federal receiver by arguing that they had an unrecorded agreement with the bank. *D'Oench, Duhme & Co. v. FDIC*, 315 U.S. 447, 459-60 (1942). In *D'Oench, Duhme*, the borrower had executed written obligations to an insured institution but claimed, after the bank failed, that the bank had orally agreed that these obligations would not be enforced. This oral side arrangement became the paradigmatic "secret agreement" barred by the doctrine enunciated in *D'Oench, Duhme*.

Since the initial statement of the doctrine in *D'Oench, Duhme*, this Court and the lower federal courts have expanded its preclusive effect well beyond the context of an oral "secret agreement" between the bank and the borrower.[1] In *Langley v. FDIC*, 484 U.S. 86 (1987), this

[1] *See, e.g., Bowen v. FDIC*, 915 F.2d 1013, 1014 (5th Cir. 1990) (alleged oral promise to extend loan barred by *D'Oench*); *Bell & Murphy & Assoc., Inc. v. InterFirst Bank Gateway, N.A.*, 894

(Continued on following page)

Court extended the doctrine to preclude a defense which is essentially the same as the affirmative Bank Tying Act claim King seeks to advance here: that the obligation to the failed bank was procured through fraud in the inducement.

In *Langley*, unwritten representations concerning the actual size of the land or the value of the mineral deposits would naturally mislead an outside examiner, who must rely on the written records of the failed institution. In the present case, it is no less true that the alleged, unwritten representations and promises would naturally mislead an outside examiner, simply because they are not reflected in the written documents contained in the bank's records. As succinctly stated by this court in *Langley*:

> Certainly, one who signs a facially unqualified note subject to an unwritten and unrecorded condition upon its repayment has lent himself to

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(Continued from previous page)

F.2d 750, 754 (5th Cir. 1990), *cert. denied*, ___ U.S. ___, 111 S.Ct. 244 (1990) (claim that bank induced borrowers to enter into an agreement through fraudulent misrepresentation and purported breach of obligations under alleged agreement barred by *D'Oench*); *Beighley v. FDIC*, 868 F.2d 776, 784 (5th Cir. 1989) (breach of contract, breach of fiduciary duty claims barred by *D'Oench*); *First State Bank of Wayne County, Kentucky v. City & County Bank*, 872 F.2d 707, 716-17 (6th Cir. 1989) (*D'Oench* barred undisclosed oral agreement regarding option to repurchase loan participation); and *FDIC v. Gulf Life Ins. Co.*, 737 F.2d 1513, 1518 (11th Cir. 1984) (waiver, estoppel and unjust enrichment claims barred by *D'Oench* in connection with suit by FDIC on interests in credit life policies).

> a scheme or arrangement that is likely to mislead the banking authority, whether the condition consists of performance of a counter promise (as in *D'Oench, Duhme*), or of the truthfulness of a warranted fact.

Langley, 484 U.S. at 93.

This Court in *Langley* did identify one exception to the broad reach of Section 1823(e), and thus, by implication, *D'Oench*, but it is inapplicable in this case. *Langley*, 484 U.S. at 93. "Where the bank engages in fraud 'in the *factum*' rather than fraud in the inducement, there is no valid obligation on the part of the borrower under the principal that fraud vitiates consent." *Kilpatrick v. Riddle*, 907 F.2d 1523, 1527 n. 6 (5th Cir. 1990), *cert. denied*, 111 S.Ct. 954 (1991). However, where as here, King knowingly executed a Promissory Note and Guaranty in favor of InterFirst, allegations of fraud or duress are simply allegations of fraud in the inducement. *Id.*

II. THERE IS NO CONFLICT AMONG THE CIRCUIT COURTS - NO OTHER CIRCUIT COURT HAS DECIDED THE ISSUE

The Fifth Circuit's decision does not conflict with any other circuit court on this issue. As King recognizes, this is the first decision by a court of appeals addressing the effect of the *D'Oench, Duhme* doctrine on a claim under the Bank Tying Act. (Pet. 8). King attempts to create a conflict among the circuits by arguing that the Eleventh Circuit in *Gunter v. Hutcheson*, 674 F.2d 862 (11th Cir. 1982), *cert. denied*, 459 U.S. 826 (1982), held that the *D'Oench* doctrine does not outweigh specific policies in

federal legislation crafted to protect investors. The only other circuit court case relied upon by Petitioner is *FDIC v. Morley*, 867 F.2d 1381 (11th Cir. 1989), *cert. denied*, 493 U.S. 819 (1989).

Petitioner's reliance upon *Gunter* and *Morley*, as resulting in a conflict with the Fifth Circuit's decision herein, is misplaced for several reasons. The most obvious reason is that neither *Gunter* nor *Morley*, squarely or in dictum, address the issue of the application of *D'Oench* to a Bank Tying Act claim. The only issue before the court of appeals in *Morley* was the district court's decision that the borrower in that case did not have standing to challenge the statutory basis for FDIC's acquisitions of his loan pursuant to 12 U.S.C. § 1823(c)(1) and (2).[2] Similarly, in *Gunter*, the issue before the court was whether alleged state and federal securities law violations and fraud claims were barred by Section 1823(e) or by federal common law. *Gunter*, 674 F.2d at 866.

The district court, *FDIC v. Gunter*, 492 F.Supp. 546 (N.D. Ga. 1980), aff'd, 674 F.2d 862 (11th Cir. 1982), *cert. denied*, 459 U.S. 826 (1982), held that, although the statutory protection of 12 U.S.C. § 1823(e) did not extend to the Gunters' fraud claim in that case, the FDIC had a

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[2] The Eleventh Circuit noted that the district court held that Section 1823(e) barred all of Morley's affirmative defenses including an alleged defense of duress. However, Morley did not pursue his argument on appeal and the Eleventh Circuit deemed such arguments abandoned. *FDIC v. Morley*, 867 F.2d at 1385 n. 5. Petitioner's reliance upon the remaining portion of the Eleventh Circuit's discussion in footnote five will be discussed by Respondent NCNB in the succeeding section.

defense to claims of fraud under a rule of federal common law which has come to be known as the federal holder in due course doctrine. 492 F.Supp. at 556. Critical to the Eleventh Circuit's discussion of the non-applicability of Section 1823(e) was its strained distinction between certain types of misrepresentations which could be construed as "agreements" and others which could not. *Gunter,* 674 F.2d at 867.

The distinction upon which the court depended in *Gunter* has now been forclosed by this Court's analysis and definition in *Langley* of the parameters of an unwritten "agreement". The court in *Gunter* did recognize that, where an obligor asserts that an oral side agreement controls the rights of the parties, those cases come squarely within the agreement language of Section 1823(e). *Id.* While the court in *Gunter* did state in dictum that " . . . we are less confident that these federal policies behind the FDIC Act outweigh the strong policies of investor protection embodied in the securities laws", the court refused to decide which policies were strongest and barred the Gunters' securities claims against the FDIC on other grounds. *Id.* at 874.

Perhaps most significantly, as recognized in *Kilpatrick,* 907 F.2d at 1528, the Eleventh Circuit's decision in *Gunter* was rendered before this Court's decision in *Langley.* The better reasoned analysis found in *Kilpatrick,* based upon this Court's definition of the term "agreement" in *Langley,* is that it is unimportant for purposes of *D'Oench, Duhme* analysis whether a case involves

securities fraud, bank tying act allegations or even RICO claims.[3] As held by the Court in Kilpatrick:

> It is not the nature or enforceability of an agreement between a bank and borrower that controls the application of the *D'Oench, Duhme* doctrine; if the agreement is unwritten, *D'Oench, Duhme* applies.

Kilpatrick, 907 F.2d at 1529; *citing D'Oench, Duhme*, 315 U.S. at 459.

Similar to the argument made by the plaintiffs in *Kilpatrick*, King contends, nevertheless, that the balancing of federal policies demands that investor protection embodied in laws relating to economic duress and securities laws outweigh federal policies behind the *D'Oench, Duhme* doctrine. (Pet. 9). The Court in *Kilpatrick* rejected that striking such a balance was required. *Kilpatrick*, 907 F.2d at 1529. Such a result is no less true in the present case for the reasons discussed by the court in *Kilpatrick*.[4]

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[3] Racketeer Influenced and Corrupt Organizations Act, 18 U.S.C. § 1961 *et seq.*

[4] The rationale for the court's conclusion in *Kilpatrick, inter alia*, was that " . . . there is a federal policy of protecting federally insured banks from the effect of unrecorded agreements. Obviously, *D'Oench, Duhme* is not designed to protect investors. The 'doctrine thus favors the interests of depositors and creditors of a failed bank, who cannot protect themselves from secret agreements, over the interests of borrowers, who can.' " 907 F.2d at 1529; citing *Campbell Leasing, Inc. v. FDIC*, 901 F.2d 1244, 1248 (5th Cir. 1990).

Finally, King can find no comfort in the analysis contained in Judge Brown's dissent in *Kilpatrick*. The present case does not require that King would have had to incorporate into the loan documents language that InterFirst was not to defraud him. Rather, to assert a claim based upon alleged agreements to do business exclusively with InterFirst, King was only required to ensure that such agreements were reflected in the loan documents. *See Howell v. Continental Credit Corp.*, 655 F.2d 743, 746 (7th Cir. 1981) (*D'Oench* not applicable where document FDIC seeks to enforce facially manifests bilateral obligations); *compare Bell & Murphy & Assoc.*, 894 F.2d at 754.

Even Judge Brown in his dissent in *Kilpatrick* recognizes that the borrowers in *Langley* could have included written representations as to the amounts of land and mineral rights in the bank records. *Kilpatrick*, 907 F.2d at 1532. By failing to ensure that the bank records in the present case accurately reflect the agreements King seeks to enforce, King lent himself to a scheme or arrangement likely to mislead bank examiners or tending to have that affect. *FDIC v. Byrne*, 736 F.Supp. 727, 732-33 (N.D. Tex. 1990) and cases cited therein.

Such action falls squarely within the policy of *D'Oench* of protecting federally insured banks from the effect of unrecorded agreements. *Kilpatrick*, 907 F.2d at 1529. The "doctrine thus favors the interests of depositors and creditors of a failed bank, who cannot protect themselves from secret agreements, over the interests of borrowers, who can." *Bell & Murphy & Assoc.*, 894 F.2d at 754. The *D'Oench, Duhme* doctrine does not deprive King of

federal statutes designed to protect investors and borrowers. Petitioner simply has deprived himself of certain affirmative claims by failing to protect himself in a manner required by the *D'Oench, Duhme* doctrine. *Cf. Campbell Leasing, Inc. v. FDIC,* 901 F.2d 1244, 1248 (5th Cir. 1990) (*D'Oench* doctrine did not deprive borrowers of property without just compensation where borrowers deprived themselves of certain defenses by failing to protect themselves in a manner required by *D'Oench*); *citing United States v. Locke,* 471 U.S. 84, 107-08 (1985) (upholding a federal provision extinguishing mineral interests for failure to make a timely annual filing).

III. KING ABANDONED ALL CLAIMS OF DURESS, SUCH CLAIMS ARE NOT SUPPORTED BY THE FACTS, AND THE CASES CITED IN KING'S PETITION DO NOT SUPPORT HIS POSITION

King's allegations and claims of economic duress are not before this court. The district court granted FDIC and NCNB's summary judgment motions on such claims and such claims were not the subject of King's appeal to the Fifth Circuit. (App. A 4a-6a; App. B 12a-15a, 18a-19a). Thus, King abandoned all claims of economic duress by not raising them on appeal before the Fifth Circuit. King cannot correct any error below by arguing that the nature of a claim under the Bank Tying Act is one of economic duress.

Assuming *arguendo* that such claims have been preserved, the merits of such claims are clearly unsupported by the King Affidavit submitted in response to NCNB's and FDIC's respective motions for summary judgment.

King's own articulation of such claims demonstrates that the "economic duress" alleged is not the type of "duress" recognized as a real defense under the Uniform Commercial Code or case law. First, King failed to come forward with any specific facts to support the broad conclusory allegation that he was forced to accept credit from InterFirst on the requirement that he not obtain any further credit from competitors of InterFirst or that he was forced to move his business from InterFirst's competitors to InterFirst. Second, nothing in the memorandum itself attached to the King Affidavit suggests that King was forced to accept the restructuring of loans to InterFirst. Third, King does not argue, and the facts do not suggest, that King was tricked into signing the Note or Guaranty in the belief that it was something other than a note or guaranty. Finally, King does not argue, and the facts do not suggest, that anyone at InterFirst physically forced him to sign the Note or Guaranty or threatened him if he did not.

In short, despite the label that King attempts to place on his claims, such claims do not fit the pattern of "duress" or other types of purported "real defenses" which arguably limit the broad scope of the *D'Oench, Duhme* doctrine. More importantly, the district court cases cited by King as explicitly or implicitly concluding that claims based upon economic duress are not barred by the *D'Oench* doctrine or 12 U.S.C. § 1823(e), in reality support rather than contradict or conflict with the Fifth Circuit's decision in this case. (Pet. 10). Further, none of the cases cited address the application of the *D'Oench, Duhme* doctrine to a Bank Tying Act claim.

All the cases relied upon by King were decided prior to this court's decision in *Langley*. This court's decision in *Langley* makes clear that claims, which are in essence indistinguishable from those made by the Langleys, are barred by the *D'Oench, Duhme* doctrine.

For instance, the issue before the court in *FDIC v. MM&S Partners*, 626 F.Supp. 681, 685 (N.D. Ill. 1985), was whether defendant's defenses of waiver and estoppel arose out of collateral agreement or whether such defenses were sufficiently removed from any agreement to permit their assertion. The district court in *MM&S Partners* looked to the Sixth Circuit's decision in *FDIC v. Hatmaker*, 756 F.2d 34 (6th Cir. 1985) for what it termed "the best explanation of which defenses are barred by § 1823(e)". *MM&S Partners*, 626 F.Supp. at 686. The court stated:

> There, the court found that the defendant could not use a fraud in the inducement defense under § 1823(e) because, unlike *Gunter*, the bank's fraud went to its future conduct.
>
> * * *
>
> When, however, the bank promises to perform in the future, for example, promising to lend the maker more money in the future, the promise does constitute a side agreement, governed by § 1823(e). The court must look at the 'essence' of the maker's defense to determine whether the defense really involves a side agreement . . .

MM&S Partners, 626 F.Supp. at 686-87. The *MM&S Partners* case did not address the issue of economic duress.

Regardless, its holding would bar any such theory in the present case based upon the facts which make up the "essence" of King's claims.

The Eleventh Circuit's footnote in *Morley*, 867 F.2d at 1385 n.5, creates the incorrect impression that *FDIC v. MM&S Partners*, 626 F.Supp. 681 (N.D. Ill. 1985) and *FDIC v. Balistreri*, 470 F.Supp. 752 (E.D. Wis. 1979) offer support for the argument that neither Section 1823(e) nor *D'Oench* bar claims such as duress. The court in *Balistreri* makes no mention of the application of Section 1823(e) or *D'Oench* to a claim of duress. There is no suggestion by the facts or discussion in *Balistreri* that the argument was even raised. The court had no difficulty in that case applying Section 1823(e) to bar defenses based on alleged oral promises that the borrower would incur no personal liability, but did not find it necessary to discuss Section 1823(e) in the context of the misrepresentation or duress claims made by the defendant in that case. The fact that the court disposed of such claims on the merits does not suggest that the court in *Balistreri* concluded that Section 1823(e) does not bar defenses such as duress.

FDIC v. Linn, 671 F.Supp. 547 (N.D. Ill. 1987), likewise fails to add support to King's claims herein. In *Linn*, defendants asserted both a defense of economic duress and an affirmative claim under the Bank Tying Act. While the court in *Linn*, in reliance upon a quote from *FDIC v. Powers*, 576 F.Supp. 1167, 1170 (N.D. Ill. 1983), *aff'd*, 753 F.2d 1076 (7th Cir. 1984), held that Section 1823(e) did not *alone* bar the defense of economic duress in that case, the court recognized that the broader scope of protection provided by *D'Oench*, as was used in *MM&S Partners*, should be considered. *Linn*, 671 F.Supp. at 555.

While faced with the opportunity to decide the application of *D'Oench* to both economic duress and Bank Tying Act claims, the court refused to do so holding that defendant's claims of duress and violations of Section 1972 failed on their merits. *Id.* at 555-56. For purposes of deciding this Petition, this Court should note that the court in *Linn* did suggest that Section 1823(e) would bar violations of the Bank Tying Act based on unrecorded agreements. *Id.* at 555 n. 16.

Finally, in *RTC v. Ruggiero,* 756 F.Supp. 1092 (N.D. Ill. 1991), the court noted as follows:

> It has not been conclusively resolved in the few decided cases on the issue (1) whether a defense of economic duress negates the requisite contract formative intent, so that neither . . . Section 1823(e) . . . nor the doctrine initially articulated in *D'Oench* . . . can ever come into play to begin with . . .

Id. at 1094. In adhering to the view expressed by the court in *Linn,* the court in *Ruggiero* held that the facts set out by *Ruggiero* did not satisfy the standard of legal duress. *Id.* at 1095. After reviewing the only relevant documents in the bank records relied upon by *Ruggiero,* the court held that Ruggiero could not make any mileage out of those documents to escape liability on the Note. *Id.* at 1097. Citing *Langley,* 484 U.S. at 90-92 and *Bowen v. FDIC,* 915 F.2d 1013, 1015-17 (5th Cir. 1990), the court stated that the key purpose of Section 1823(e) and *D'Oench* "is to ensure that bank regulators (including takeover government agencies such as RTC) can comfortably rely on the regulated financial institution's official records." *Ruggiero,* 756 F.Supp. at 1097. The court concluded that the scenario painted by

Ruggiero was a classic one for the defeat of the borrowers claims. *Id., citing Bell & Murphy & Assoc.*, 894 F.2d at 753-54.

This case does not present a significant unanswered question regarding the scope of the *D'Oench* doctrine as the Fifth Circuit's decision is well within its scope and this court's decision in *Langley*. The policy of protecting the FDIC and its assignees would be undermined by allowing defenses or counterclaims based on alleged Bank Tying Act violations that involve an unrecorded agreement between a borrower or obligor and the failed bank.

CONCLUSION

The Petition for Writ of Certiorari should be denied.

Respectfully submitted,

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